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As China Invests, U.S. Could Lose

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Report on Chinese Investment

SHANGHAI — For three decades, wealthy nations have invested hundreds of billions of dollars in China, helping drive one of the most remarkable economic booms in history.

Now, China is poised to return the investment favor. The question is whether the United States will be willing and able to fully participate, according to a new study to be released Thursday.

Flush with capital from its enormous trade surpluses and armed with the world's largest foreign exchange reserves, China has begun spreading its newfound riches to every corner of the world — whether copper mines in Africa, iron ore facilities in Australia or even a gas shale project in the heart of Texas.

The study, commissioned by the Asia Society in New York and the Woodrow Wilson Center for International Scholars in Washington, forecasts that over the next decade China could invest as much as \$2 trillion in overseas companies, plants or property, money that could help reinvigorate growth in the United States and Europe.

But the report, to be released at a Washington news conference that Commerce Secretary Gary Locke plans to attend, also warns that the United States risks missing out on a large

share of the Chinese investment boom because of politics, a growing rivalry between the two nations and deep-seated perceptions that Chinese investments are unwelcome in America.

“If political interference is not tempered,” the study warns, some of the benefits of Chinese investment — “such as job creation, consumer welfare and even contributions to U.S. infrastructure renewal — risk being diverted to our competitors.” While Wall Street banks have lobbied for more Chinese investments in the United States, hoping that will bring bigger deals for the banks, Washington has remained wary — even though the Obama administration says it welcomes Chinese money.

But anti-China rhetoric is hot in Washington and among many state and local officials.

One frequently cited worry is that Chinese companies, many of them owned partly or entirely by the government, will use their purchases to gain military secrets. Another concern is that Chinese companies will buy American companies with manufacturing operations in the United States, close those factories and move production to China.

China, of course, is already a force in global markets. Over the last few years, it has made multibillion-dollar loans to developing nations and let its state-owned companies acquire minority stakes in global powerhouses like Rio Tinto, Morgan Stanley and the Blackstone Group.

China is also a major player in the global debt markets, holding about \$1.6 trillion in United States Treasury bonds, an investment that helps keep American interest rates low and finances America’s enormous debt.

But China is still a relatively small player in overseas direct investments, which include purchases of large, voting stakes in foreign companies and plants. That also includes investments in new construction projects on previously undeveloped land — so-called greenfield facilities.

Last year, China’s overseas direct investments amounted to about \$59 billion. By comparison, the United States’ figure was over \$300 billion.

But with Beijing pushing its big companies to go overseas and invest in resources and technology, China’s investments could soon reach \$100 billion to \$200 billion a year, according to the Asia Society study.

The potential problem for Beijing is that Chinese companies are not always welcomed overseas — not only because China wields enormous economic clout but because state-owned giants are believed to be subsidized by the state and possibly working in the interest of the government.

Congressional critics of China's investment aspirations include Senator Jack Reed, Democrat of Rhode Island. "Many of these companies are so closely intertwined with the government of China that it is hard to see where the company stops and the country begins, and vice versa," Mr. Reed recently told Reuters.

A series of proposed Chinese deals in the United States have been blocked by regulators or attacked by local politicians, who say they are worried China could gain access to sensitive military technology or take control of valuable natural resources.

In 2005, one of China's giant oil companies, Cnooc, dropped its bid to acquire the American oil giant Unocal after a Congressional investigation into the purchase. And in recent years, the Chinese telecommunications giant, Huawei, has repeatedly been rebuffed from making deals in the United States, over national security concerns.

More recently, the Anshan Iron and Steel Group, a Chinese company seeking to build a relatively unsophisticated steel rebar factory in Mississippi, had to fight fierce political opposition in the state, including fears the project would result in job losses and threaten national security.

Angered at what it says is protectionism masquerading as national security concern, Beijing has lodged sharp complaints with Washington.

The Treasury Department has placed the topic on the agenda for a high-level dialogue with Chinese officials scheduled for next week in Washington.

"We strongly welcome investment from around the world, including China," says Lael Brainard, one of the highest-ranking Treasury Department officials.

Still, some experts say anti-China sentiment is so high across the country that the United States is unlikely to attract the huge investments over the next few years that the Asia Society study suggests are possible.

"There's no chance this is going to happen," says Derek Scissors, an expert on China at the Heritage Foundation, a conservative policy institute in Washington. "They want to invest a

lot, but no one here's going to let them. The political climate in Washington is too anti-China right now.”

Daniel H. Rosen, co-author of the study with Thilo Hanemann, and a principal at the Rhodium Group, an economic advisory firm in New York, says that if Chinese companies are turned away, it could significantly reduce investment opportunities in the United States.

And, he warns, it could prompt China to retaliate against American businesses that operate in China, while also discouraging Beijing from pushing ahead with reforms that would make its business and financial markets more open and transparent.

“America has been debating this kind of thing for hundreds of years,” Mr. Rosen said. “But time and time again, America has decided” to be open to investment from overseas, he said. “Our conclusion is China is no different.”

To ensure that America gets its share of China's money, the study calls on Washington to send a clear, bipartisan message that Chinese investment in the United States is welcome, to protect any national security review process from political interference and to work with China to enhance its own transparency when it proposes investing in the United States.

Some analysts say China deserves some of the blame for opposition to its overseas investments, not just in the United States but elsewhere.

Chinese companies are not very transparent, and much of the investing by China is done by a handful of government-owned companies that have access to cheap state financing, giving them what some analysts say is an unfair advantage in competing for resources or assets.

But many analysts say China and the United States clearly need each other. China now has the capital American business so desperately seeks, and the United States has technology and a highly skilled work force.

Orville Schell, director of the Center on U.S.-China Relations at the Asia Society and the person who commissioned the study, says the United States must do its part to improve relations with China.

“I feel increasingly alarmed and discouraged by the willful ignorance of Americans to the competitive challenge the Chinese pose to the U.S., including in foreign investment,” Mr.

Schell said in an interview. “China is looking for places to park its money, and it could be to our advantage. If we don’t find a way to be open to China, it’s undeniable the money will go elsewhere.”